Canadian Superior Oil Ltd. Annual Report 1973

AR20

Canadian Superior Oil Ltd.

Incorporated under the Laws of Canada

Head Office: Three Calgary Place,
355 Fourth Avenue S.W.,
Calgary, Alberta T2P 0J3

Directors

D. L. BOHANNAN, Calgary, Alberta
H. J. CAINE, Calgary, Alberta
A. E. FELDMEYER, Calgary, Alberta
T. F. C. FROST, London, England
D. C. L. JONES, Calgary, Alberta
H. B. KECK, Los Angeles, California
W. M. KECK, Jr., Los Angeles, California
J. L. NORMAN, Houston, Texas
J. W. PYLE, Calgary, Alberta
W. G. ROBINSON, Vancouver, British Columbia

Officers

A. E. FELDMEYER, President
D. L. BOHANNAN, Vice-President, Operations
H. J. CAINE, Vice-President, Exploration
T. J. EMERSON, Vice-President, Contracts
D. C. L. JONES, Vice-President, Secretary and General Counsel
J. W. PYLE, Vice-President, Finance and Administration
R. C. SCHRADER, Vice-President, International Contracts
E. J. BETHELL, Treasurer
R. G. CHITTICK, Comptroller
R. C. MACDONALD, Assistant Secretary
D. J. PARKHILL, Assistant Secretary

Auditors

PRICE WATERHOUSE & CO.,
Calgary, Alberta

Transfer Agents

THE ROYAL TRUST COMPANY
Calgary, Alberta; Vancouver, British Columbia; Winnipeg, Manitoba; Toronto, Ontario; Montreal, Quebec; Saint John, New Brunswick; and Halifax, Nova Scotia.

THE BANK OF NEW YORK
New York, New York 10015

Registrars

THE ROYAL TRUST COMPANY
Calgary, Alberta; Vancouver, British Columbia; Winnipeg, Manitoba; Toronto, Ontario; Montreal, Quebec; Saint John, New Brunswick; and Halifax, Nova Scotia.

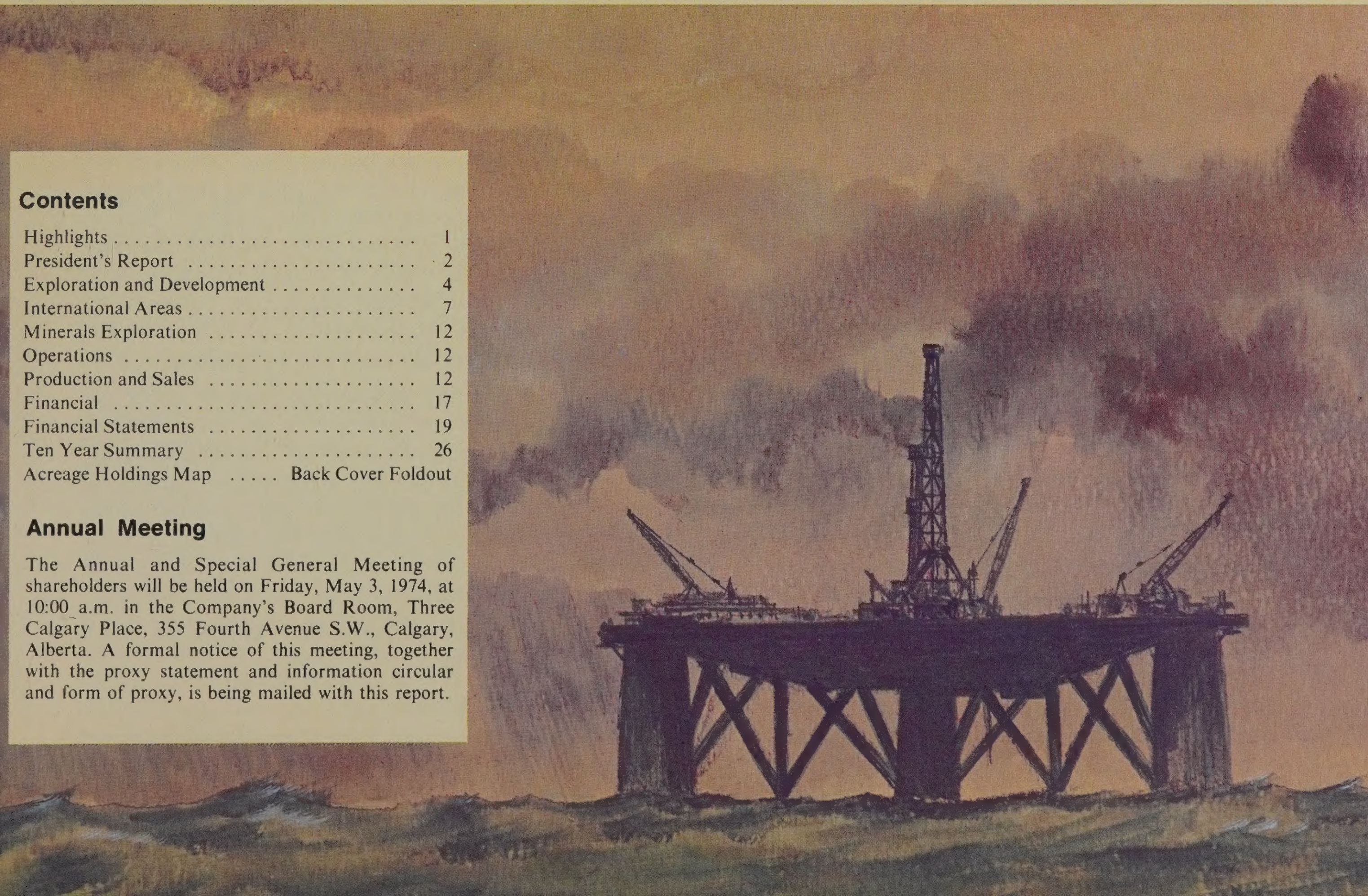
FIRST NATIONAL CITY BANK
111 Wall Street
New York, New York 10015

Stock Exchange Listings

AMERICAN STOCK EXCHANGE (CDS)
PACIFIC STOCK EXCHANGE (CDS)
TORONTO STOCK EXCHANGE (CAS)

Highlights

	1973	1972
Gross Revenue	**$63,007,158**	$46,397,060
Working capital provided from operations—*before drilling and exploration expenditures*	**$36,399,223**	$26,994,906
Per Share	**$4.27**	$3.17
Net Income	**$12,338,013**	$ 6,618,603
Per Share	**$1.45**	$ .78
Working Capital at Year End	**$18,636,258**	$16,974,402
Average Net Daily Sales:		
Crude Oil (Bbls.)	**24,562**	23,036
Condensate (Bbls.)	**7,079**	7,472
Propane and Butane (Bbls.)	**4,129**	4,609
Total Oil and Gas Liquids	**35,770**	35,117
Residue Gas (Mcf)	**203,985**	162,632
Sulphur (Long Tons)	**593**	504
Net Acreage in Canada	**9,453,985**	10,048,035
Net Acreage — Foreign	**7,765,674**	7,735,359



Contents

Annual Meeting

The Annual and Special General Meeting of shareholders will be held on Friday, May 3, 1974, at 10:00 a.m. in the Company's Board Room, Three Calgary Place, 355 Fourth Avenue S.W., Calgary, Alberta. A formal notice of this meeting, together with the proxy statement and information circular and form of proxy, is being mailed with this report.

President's Report

To The Shareholders:

Financial

1973 was a year of strong financial gains for your company. Income from all sources increased 36% to $63 million, primarily due to higher product prices. Working capital provided from operations (cash flow) before drilling and exploration expenditures amounted to $36.4 million or $4.27 per share compared with $27 million or $3.17 per share in 1972. Net income amounted to $12.3 million, equivalent to $1.45 per share compared with $6.6 million or $.78 per share in 1972.

Because of the attention focused on the energy crisis and the higher profits reported by industry, criticism has been levelled at what has been referred to as "windfall profits". More meaningfully, Canadian Superior's net income for 1973 represented a rate of return on invested capital of 9.5% compared with a rate of return for the prior year of only 5.3%. In times of drastically escalating costs of finding new reserves of oil and gas, these rates of return can indeed be considered modest in a high-risk industry. As a matter of fact, both the economic and political climate must improve for industry to attract the vast sums of capital necessary to meet the growing energy needs in Canada and the free world.

Canadian income taxes paid to federal and provincial governments amounted to approximately $11 million, which when added to those taxes deferred in 1973 of approximately $1 million, accounted for a charge against income totalling $12 million and represented a 69% increase over the prior year.

It is of interest to note that, in addition to income taxes paid to government, approximately $11.2 million was paid by Canadian Superior by way of royalties, mineral taxes, rentals, bonuses, and property taxes to municipal, provincial and federal governments in Canada during 1973. This does not include other indirect taxes, such as sales and excise taxes added to the cost of materials utilized by the Company.

Expenditures for oil and gas properties totalled $7.6 million, of which $5.7 million or 76% represented expenditures outside of Canada, primarily in the offshore Gulf Coast areas of Texas and Louisiana.

Drilling expenditures during 1973 amounted to $8.3 million, approximately 8% higher than those of the prior year. Drilling in areas outside of Canada increased 38% as opposed to a marginal reduction of expenditures in western Canada. Geological and geophysical expenditures outside of Canada more than doubled, while expenditures within Canada declined 15%.

Exploration in Canada is becoming less attractive than in certain other regions of the world where the company is searching for new reserves of hydrocarbons. There are several reasons for this trend. The discovery ratio is diminishing in Canada, making new reserves more costly. The controlled lower domestic price of crude oil in contrast to higher prices available elsewhere in the world and the impact of increased domestic taxes and royalties are further inhibiting factors. Furthermore, the stable policies of government are being replaced by trends which are arbitrary and inflationary.

The trend over the past several years of major gas plant construction and additions to present productive fields in Canada has now peaked out with the completion of the new sales gas facilities expansion at Harmattan. This accounts for the reduction of plant and equipment expenditures to $5.8 million from $11.1 million in 1972. Further reductions are anticipated for 1974 in this area of capital expenditures.

Working capital increased $1.7 million to $18.6 million at year end.

Production and Revenues

Sales of crude oil and natural gas liquids increased marginally to 35,770 barrels daily. Crude oil production

increased approximately 7%; condensate, propane and butane dropped approximately 7%; attributable largely to a fire at the Harmattan plant in April resulting in approximately three months' down-time. This loss was covered by insurance. Revenues after royalties from oil and liquid product sales amounted to $43.8 million, an increase of 30%.

Natural gas sales during 1973 averaged 204 million cubic feet daily, an increase of 25% over the prior year. Revenue from gas sales increased 46%, due in part to higher prices.

While sulphur production declined approximately 13% to 779 tons daily, sales increased 17% and revenues improved 61% to $1.2 million, reflecting a marked and continuing firming in sulphur prices and a significant rise in demand.

Exploration and Drilling

The expenditure figures mentioned previously are indicative of the exploration activity within Canada and the increased tempo of exploration in other geologically promising areas elsewhere in the world.

Canadian Superior participated directly or indirectly in the drilling of 129 exploratory and development wells in Canada, 39 in the Offshore Gulf Coast area of Texas and Louisiana, 2 wells in the United Kingdom sector of the North Sea, and one in the Sulu Sea, Philippines area. Ninety-two wells were productive of oil and gas and 79 were abandoned. Sixty-seven of these wells were drilled under farmout agreements at no cost to the company.

Canadian Superior acquired a 6% interest in a block in the High Island area in Offshore Texas and retroactively acquired varying interests of ¾% to 1½% in eleven other blocks awarded at the June 19th, 1973 Federal Lease Sale in Offshore Texas. An exploratory program has commenced on several of these blocks. Participation in exploration and development in the Gulf Coast area and revenues derived therefrom are expected to play an increasingly significant part in Canadian Superior's overall operations.

Outlook

A great many economic and political uncertainties have arisen which vitally affect our industry. Governmental interference in the interplay of the free enterprise forces of supply and demand by way of the implementation of export taxes on oil, and the steeply higher royalties (discussed elsewhere in this report) act as deterrents to financing the growing needs for investment capital. It is not known at this time what portion, if any, of the export tax levied by the Canadian federal government will accrue to industry. We trust that federal and provincial governments will soon recognize that the oil industry is living off inventories of relatively low-cost energy, and replacing those reserves has become extremely costly. New reserves will only be discovered if rates of return are commensurate with the risks involved.

Employees

The will to overcome the present uncertainties and to meet the many challenges ahead rest upon the strength and competence of our employees, to whom we take this opportunity to express continued confidence and appreciation.

ON BEHALF OF THE BOARD,

A. E. Feldmeyer

March 9, 1974 President

Exploration and Development

CANADIAN SUPERIOR'S CANADIAN ACTIVITIES

Canada

During 1973 your company participated in seismic programs in the deep foothills belt of Alberta and has continued seismic operations in the Mackenzie Delta region of the Northwest Territories. The drilling of shallow-gas prospects in southeastern Alberta and southwestern Saskatchewan, both by your company alone and with others, has been intensified.

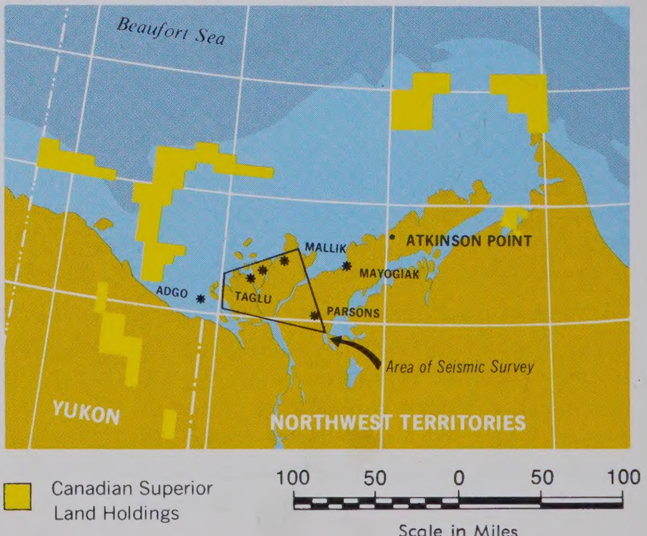
The company participated in drilling 75 exploratory wells in Canada in 1973, of which 17 resulted in discoveries.

Canadian Arctic

Except for a small participation in a deep test well at Drake Point on Melville Island, no exploration was carried out by the company in Arctic regions, nor have any plans been made to drill on Canadian Superior's Arctic properties during 1974. Drilling in the Beaufort Sea area will be deferred until 1976 at the earliest until industry and government have conducted extensive ecological studies, and regulations governing operations in this sensitive region have been formulated.

Mackenzie Delta

The company, as operator of a five-company group, conducted a geophysical survey in the Mackenzie Delta area to gather data on this attractive geological area



and obtain information which could lead to acquisition of acreage, either by farmin or purchase of rights at Federal government sales. During 1973 some 380 miles of seismic data was shot and an additional 1,280 miles were acquired through purchase and participation surveys at a cost to the company of $474,000. The program will continue during 1974.

Grant Lands

When the company amalgamated with the Calgary & Edmonton Corporation in 1966 it acquired in excess of one million acres of fee lands in Alberta located in two general areas north and south of Calgary and referred to as North Grant Lands and South Grant Lands (see map).

In the South Grant Lands block, an agreement has been made with a major company to carry out an extensive seismic evaluation program. Depending on the results of the survey that company may commit to the drilling of three deep wells. This South block contains attractive deep prospects which have been lightly explored and the present energy demand has enhanced the economic aspects and will justify more detailed examination.

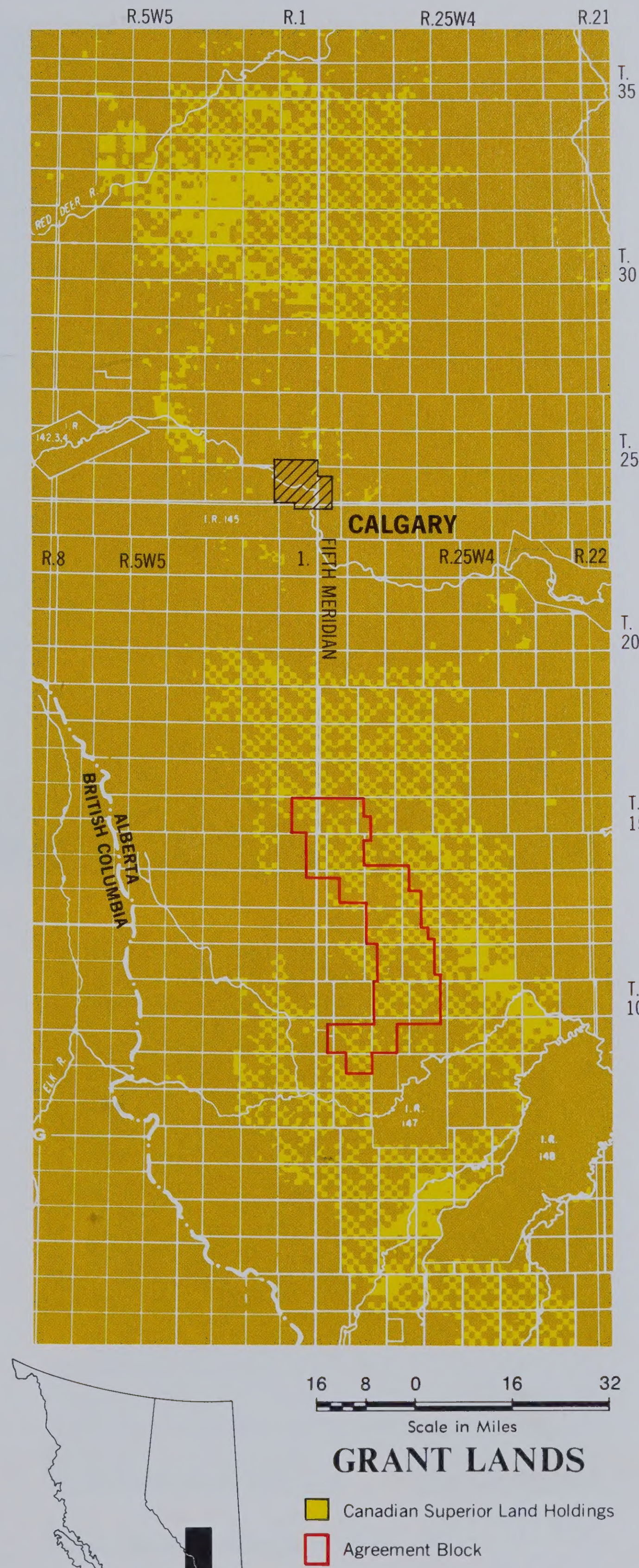
In the North Grant Lands block, an oil drilling program in which your company has a 50% participation, is underway in the Twining region. A four-well program on wholly-owned lands is planned for the Garrington area as a follow-up to a recent oil development completed by another company in which Canadian Superior has a royalty interest. As a result of changes in prorationing and increased allowables in this area, your company has made several farmouts and increased activity is anticipated.

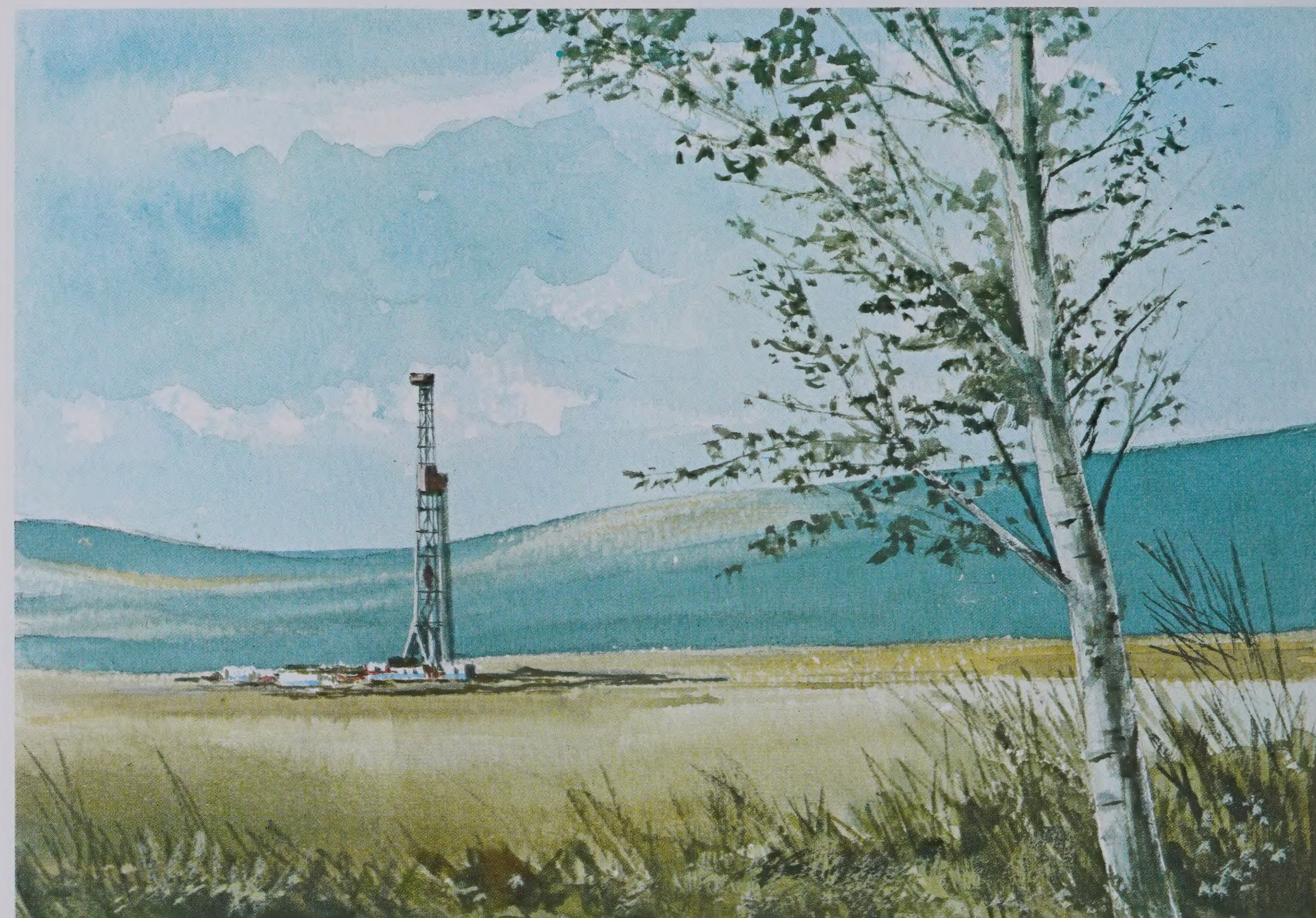
Southeastern Alberta - Southwestern Saskatchewan

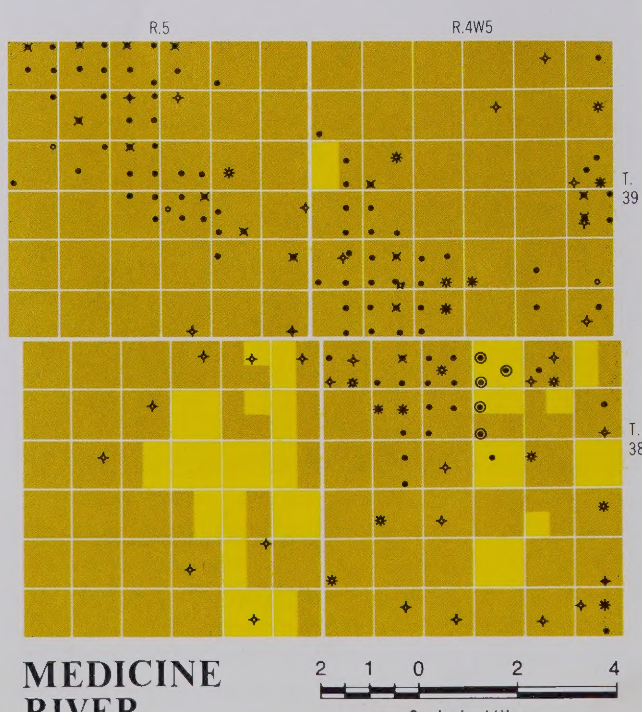
The drilling of 20 wells to develop low pressure gas reserves on a farmout of company acreage in the general Medicine Hat area was essentially completed in 1973. Considerable price escalation has occurred in recent months and more is expected during 1974. This provides a satisfactory economic environment for the ultimate marketing of these reserves.

Other Areas

A wholly-owned gas well was completed successfully on the north edge of the Olds field. Infill drilling was also continued to improve field productivity in the Steelman unit in Saskatchewan as well as in the Norbuck, Rosebank, Ferrier, Lookout Butte, Carstairs, Ghost Pine, and Kaybob areas of Alberta; and at Inga in Northeastern British Columbia.







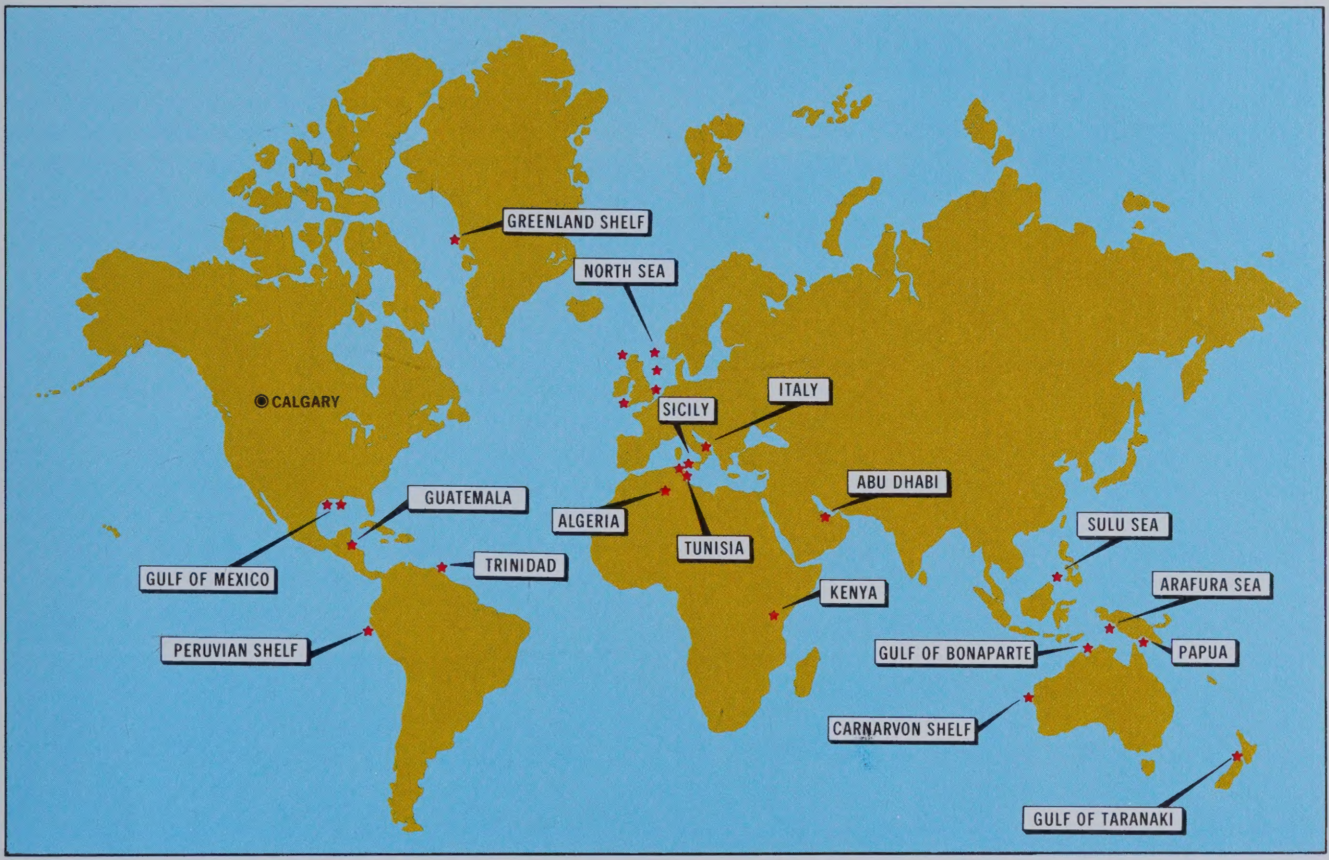
Medicine River

In the Medicine River area of south-central Alberta your company has participated in the discovery and development of significant oil and gas reserves. Five multizone oil and gas wells have now been completed and further drilling is in progress. Your company's interest varies from 33-1/3% to 100%.

Land Holdings in which the Company has Varied Interests.

Recent Discovery Wells.

CANADIAN SUPERIOR'S INTERNATIONAL ACTIVITIES

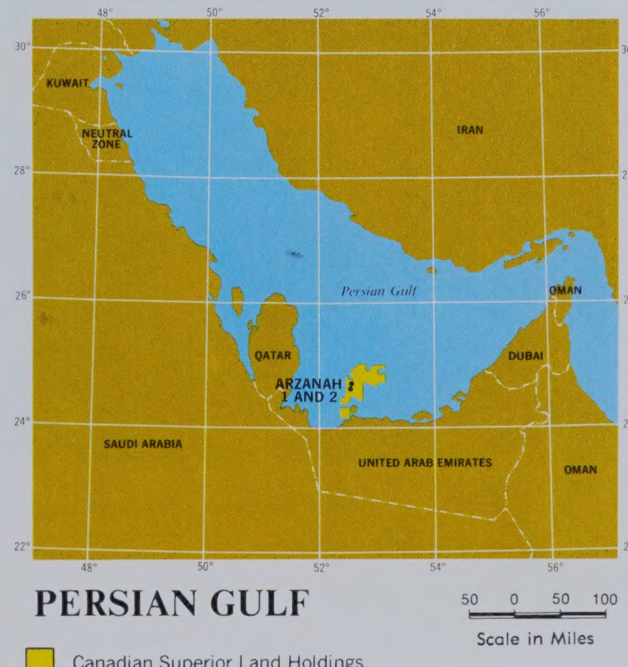


International Areas

Canadian Superior continues to increase its scope of international operations and is represented in many countries in exploration permits involving joint participation with other companies. The majority of these concessions lie offshore on continental shelves where initial exploration involves marine seismograph surveys. In addition to permits previously held, agreements have been negotiated during the past year in several other prospective areas.

Abu Dhabi

During August, your company entered into an agreement involving the drilling of a wildcat well in offshore Abu Dhabi in the Persian Gulf area. The initial well discovered light gravity oil with a potential production capacity in excess of 4,000 barrels per day. A stepout well, located three and one-half miles south southwest from this discovery, is now drilling and initial testing indicates an extension of the oil pool. Canadian Superior will earn a 10% working interest upon completion of the terms of the agreement.



PERSIAN GULF

Kenya

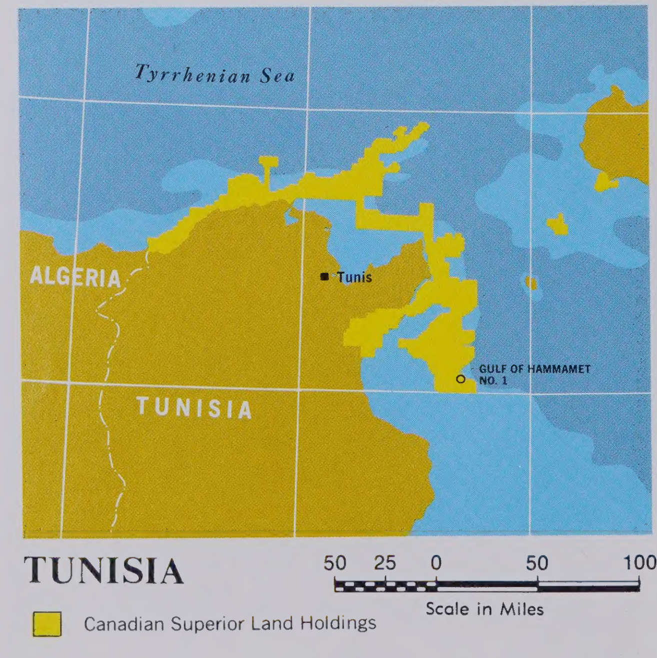
During the fourth quarter a geological mapping and sampling program was conducted related to our oil exploration license in the Tana River area of Kenya. Approximately 968 miles of seismic data were processed and reinterpreted and geochemical studies are in progress on samples collected from this survey. Further geophysical projects during 1974 will be contingent on the results of this data.

Nigeria

Your company, as a member of a group, has obtained an option to drill on an offshore license pending a satisfactory examination of available seismic and geological information. The license is located in an excellent prospecting area in the Niger Delta region.

Tunisia

Additional areas were obtained which extended the company's concession in the Hammamet Gulf. Seismic surveys were completed and a well, in which Canadian Superior has a 15% interest, commenced drilling in November, 1973. The well is projected for 15,000 feet and is currently drilling above its objective depth.



Guatemala

A farmin has recently been obtained on acreage in the Gulf of Honduras, offshore Guatemala in Central America, where previous geophysical surveys indicated two anomalies. Two wells are scheduled to be drilled within the next few months and Canadian Superior will earn a 12½% interest in the acreage in return for assuming 25% of the costs.

Italy

Seismic surveys have been conducted over two permits held offshore south of Sicily and over two onshore permits in the Calabria area of southern Italy. Interests vary between 20% and 25%. An application for a permit onshore Sicily has been approved and your company, with a partner, has been granted five permits offshore western Italy. Applications have been approved for exploration permits in which Canadian Superior's interest is 25%, near the Italian controlled island of Lampedusa in the Central Mediterranean.

Philippines

In the Sulu Sea area of the Philippines your company is participating in drilling a well which will earn it a net 5% interest in a production-sharing contract involving 3,935 square miles. An equivalent interest in an adjoining contract consisting of 2,250 square miles can be earned by the drilling of a second well.

Indonesia

Your company farmed out its interest in the 70,000 square-mile concession in the Arafura Sea. Under the terms of the agreement the earning company must spend $4 million to earn a 25% interest in the concession and Canadian Superior's interest will be reduced from 10% to 5%. During 1973 the farmee carried out a 2,412 mile marine seismic survey and this will be followed by an onshore seismic survey on Aru Island. In addition a 12,000 foot well is scheduled for the third quarter of 1974.

New Zealand

Canadian Superior in partnership with others negotiated a farmin to earn a 40% interest in a 5,928 square mile offshore concession in the Gulf of Taranaki. The area is located north of the South Island and adjoins the Maui gas and condensate field. An offshore drilling rig, currently under construction in Singapore, will be used to drill two earning wells and drilling is expected to begin during the last quarter of 1974.

CANADIAN SUPERIOR'S AUSTRALASIAN ACTIVITIES

Australia

Canadian Superior's net acreage position in three separate permits in Australia's western and northwestern shelf area remained unchanged. The year's only activity was limited to seismic surveys. It is anticipated that at least two of the permits will be relinquished during 1974, reducing our net acreage to about half of the current figure. Current Australian government policies are unfavourable for continued exploratory drilling.

Papua New Guinea

In December, 1973 Papua New Guinea became an independent nation. Canadian Superior has maintained its 15% working interest in six permits in the Gulf of Papua and during the year 2,454 miles of marine seismic was carried out to evaluate the deeper Mesozoic beds. As a result, at least one deep Mesozoic test will be drilled in the latter half of 1974.

NORTH SEA AREA

North Sea

During the past year an exploratory well was drilled and abandoned on Block 30/23. Three exploratory tests were also drilled on Block 49/28, in which your company holds a 3-1/3% interest; two of which were completed as gas wells, one with a potential of 60 million cubic feet per day.

We anticipate exploratory drilling on the blocks east of the Shetland Islands will get underway about May, 1974. Canadian Superior's interest is 8%.

Expansion of production facilities in the Hewett and Leman fields continued during 1973. The company's share of revenue from these fields amounted to $917,500; an increase of 17% over the previous year.

A group, in which Canadian Superior has a 12½% interest, has submitted applications for licences in the Norwegian sector of the North Sea and awards are expected during the current year.

United States - Gulf of Mexico

At a Federal Lease Sale on June 19th in the Galveston and High Island area Offshore Texas the company was successful in bidding on Block A-337 to acquire a 6% interest. Canadian Superior retroactively acquired interests from ¾% to 1½% in 11 blocks awarded at the same sale. Exploratory drilling is currently underway on several of these blocks. As at March 1st, 1974 five

GULF OF MEXICO

wells had been completed with hydrocarbon discoveries announced on Blocks A-323 and A-555. Six other locations are either drilling or authorized but further information is being held confidential in view of the expected Federal Lease Sale in May, 1974.

A Federal Lease Sale is also scheduled for Offshore Louisiana in March and a group, in which Canadian Superior holds a 5% interest, is evaluating the prospects.

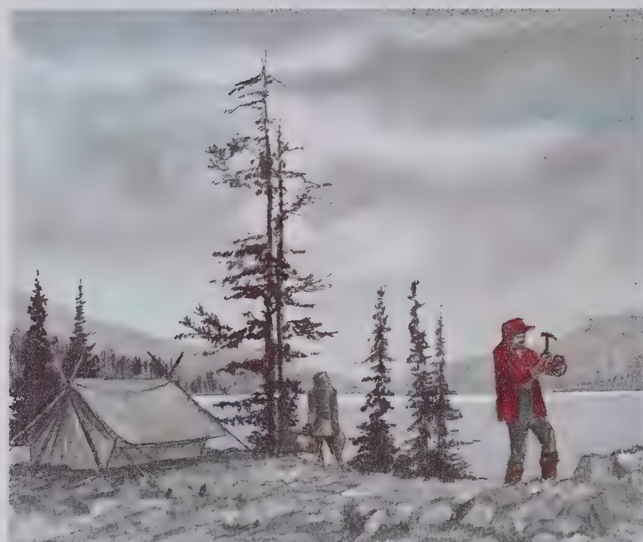
Another Federal Lease Sale Offshore Texas is scheduled for the fourth quarter of 1974 and a group, in which your company has a 15% interest, is well advanced with geological and geophysical evaluations of the area.

Development of Eugene Island Blocks 296 and 306 (Offshore Louisiana) proceeded steadily during 1973. Block 296 is now approaching the fully developed stage with 40 wells on stream. Production from Block 306 commenced January 23, 1974. Nine wells are now on production and drilling has begun from the second platform. Revenue for 1973 from Block 296 amounted to $780,000. Combined revenue from Blocks 296 and 306 should approach $2 million for 1974 for our 5% and 5.6% interests, respectively.

Six wells have been drilled on Block 249 and four on Block 250 in the South Marsh Island Louisiana area. A commercial gas field is indicated but information is being held confidential due to the pending Federal Lease Sale in March. Canadian Superior holds a 7% interest in this area.

Production from Brazos Block A-1 (Offshore Texas) commenced on August 23, 1973 and revenue from this field amounted to just under $70,000 for 1973. Revenue for 1974 should approximate $250,000 for the company's 5% interest.

Minerals Exploration



Canadian Superior Exploration Limited was active in British Columbia, the Yukon, the Northwest Territories, Idaho, Montana and Ireland during 1973. Work was carried out on 19 properties acquired by staking or by government permits and on 8 properties held under option. Nine properties were tested with diamond drill holes. Exploration expenditures totalled $889,000 during the year and we are pleased to report some modest success. A one-sixth interest is held in a copper property in the Yukon which indicated commercial possibilities. A 22¼% interest is held in a gold-silver property in southern Idaho, which is responding favourably to drill hole testing. A one-sixth interest is held in permits on the Arctic Islands on which lead-zinc mineralization has been discovered.

In Australia, the company was involved in exploration projects for uranium in the Northern Territories and in Western Australia. Further exploration was carried out on five nickel properties in Western Australia. Your company has a 50% interest in a high-quality limestone deposit in Papua which is being considered as a source of raw materials for the cement industry of Australia. Canadian Superior's share of expenditures in Australia during 1973 totalled $156,000.

Operations

Gas Plants

Gas sales facilities for the Harmattan East field in Alberta were completed during 1973. The plant is designed to condition gas to meet an approved sales volume of 60 million cubic feet a day. The company's interest is approximately 43%.

The expansion of the Innisfail D-3 Unit conservation gas processing facilities was completed at mid year. The enlarged facilities are designed to process the sour solution gas associated with oil production of 13,600 barrels per day compared with previous production of 10,000 barrels daily. Your company's interest is 33%.

Production and Sales

Oil and Condensate

Production of crude oil and natural gas liquids in Canada increased marginally to an average of 35,637 barrels per day in 1973. Increased prices received in Canada were influenced by a threatened shortage of foreign crude supplies to North America coupled with a significant escalation in foreign prices. In January, crude oil and condensate prices in Canada increased by 20c per barrel. In May, further increases of 25c and 35c per barrel for crude oil and condensate respectively were received. Finally, in August, prices again increased by 40c per barrel for crude and 50c per barrel for condensate. Further increases to the producers ended when the federal government, during September, implemented a price freeze on crude oil and refined product prices until April 1, 1974 at which time the government is expected to announce its pricing policy.

On March 1, 1973 the federal government began licencing exports of crude oil and condensate leaving Canada. On October 1st an 'export tax' of 40c per

barrel was imposed on crude oil and condensate shipped to the United States. The export tax rose to $1.90 during December; to $2.20 during January, 1974 and to $6.40 during February, 1974. The reasons given for imposing the export tax were to obtain the prevailing market price outside of Canada and equalize prices east of the Ottawa Valley, while ensuring that the producer-owners of the crude did not obtain 'windfall' profits. No intimation has been given as to what may be considered 'windfall' profits. Neither has there been any freeze, either voluntary or mandatory, on the prices of the many commodities, equipment and supplies which oil and gas companies require to carry out their operations.

Although price increases received during 1973 significantly improved gross revenues, they were modified by increased oil royalties imposed by the provinces of Alberta and British Columbia, as well as by a new mineral income tax in Saskatchewan. The full benefit of the price increases effected during 1973 will be reflected in 1974 income. But again, still higher royalty rates proposed by the province of Alberta to be effective in 1974 will modify the benefit. At the time of this writing new royalty schedules for oil had not been announced.

Natural Gas

The company's natural gas sales in Canada in 1973 averaged 189 million cubic feet per day, a 22% increase over 1972. Most of the increased sales were from the Harmattan fields where additional facilities began operating in late 1972 and during 1973. A gas peaking arrangement was negotiated with TransCanada PipeLines Limited and became effective September 1, 1973. This allowed the operator to build excess capacity and provide the purchaser with flexibility to take large volumes in periods of peak demand. Under the arrangement, the purchaser contributes toward the excess costs of the expanded facilities.

The increasing demand in North America for natural gas and the shortfall in sufficient new sources of supply has brought about an acknowledgement that natural gas has been significantly underpriced in the market place. The result has been escalating prices and pressure for further development. This trend is expected to continue into the foreseeable future.

The company negotiated price increases on substantially all of its gas sales contracts, the majority of which became effective in the latter part of 1973.

Alberta and Southern Gas Company Ltd. has recently announced an increase effective July 1, 1974 which would, if accepted, approximately double the present contract prices. Sales to that company represent about 16% of total sales. This gas goes entirely into the export market to United States purchasers. TransCanada PipeLines Limited, which markets most of its gas in Canada, has offered a less favourable price increase which is now being evaluated.

Effective January 1, 1974 a new Crown royalty schedule in Alberta, applicable to old gas, will significantly increase the government's share of production. A basic rate of 22% will apply to the first 26c per thousand cubic feet of field price. Increased royalty applied on a sliding scale will bring the effective rate to 25.6% at a field price of 36c and to 34.3% at 56c. The revised royalty rate on new gas, defined as gas produced from a new pool discovered by a well licenced after January 1, 1974, escalates at a somewhat lower rate above the 22% basic royalty.

Liquified Petroleum Gases

The continuing increase in the use of LPG's resulting from an over supply and resultant low prices in comparison to other fuel sources, has finally brought about a failure of supply to meet all of the growing demands of the market place. Consequently, there has been a sharp increase in the price levels. The premium value of this clean-burning fuel, plus its increasing use in refining and petrochemical processing, will continue to add pressure on both supply and price. Unlike natural gas, LPG's have transportation and distribution flexibilities that make them an extremely versatile commodity.

Approximately one-half of Canada's production of liquified petroleum gas is excess to Canadian requirements and over the past decade markets for most of this surplus have been developed in the United States. During the later months in 1973 the federal government, expressing concern for future Canadian needs, imposed licencing procedures on exports and established minimum export prices.

In late December, propane producers acceded to the request of the Alberta government to roll-back their prices for sales in the province to October, 1973 levels in order to help relieve the impact of price increases being experienced by Alberta consumers. The conflict between federal policy of securing maximum prices in the export market and provincial policy of maintaining the lowest possible prices in the Alberta market has caused a great deal of confusion and difficulty for propane producers.

Canadian Superior's propane and butane sales volumes decreased by 10.8%, primarily due to a fire in late April at the Harmattan Area Plant. In spite of this lost volume, however, sales revenue increased by 67% to $3.6 million as a result of higher prices.

Although propane and butane prices are expected to remain at a more acceptable level, the new royalty schedules proposed by the Alberta government will have an adverse effect on these revenues during 1974.

Sulphur

Sulphur prices began to improve in 1973 in response to increasing demand and improved prices for fertilizer. The industry is currently unable to meet the requirements of the offshore market due to transportation equipment shortages and marine terminal capacity limitations. Supply of liquid sulphur for Canadian and United States requirements is also limited by the availability of rail-connected production. Solutions to both problems will require large capital investments and significant lead time and as a result the tight supply market and price escalation is expected to persist. Aside from transportation problems, continued strong demand could be met by breaking up and melting old sulphur from block storage; but prices have not yet reached a level high enough to justify this costly procedure.

Sulphur production averaged 779 long tons per day, a decrease of 13% brought about by declining production. Sulphur sales volume increased 17% while revenue from sales amounted to $1.2 million, an increase of 61%. In 1974 improved prices will become effective as existing contracts expire.

Oil and Gas Acreage Holdings

	Gross		Net	
CANADA				
Producing leases		675,295		345,340
Exploratory acreage:				
Western Canada				
Leases	2,759,712		1,960,736	
Reservations and permits	1,812,363		1,061,255	
Fee title acreage	1,309,638	5,881,713	1,309,282	4,331,273
Yukon and Northwest Territories				
Leases	105,567		27,148	
Permits	1,414,036	1,519,603	672,512	699,660
Beaufort Sea		4,134,266		1,818,967
Mackenzie Delta — onshore		492,343		246,172
Arctic Islands				
Leases	75,303		1,883	
Permits	1,053,925	1,129,228	484,137	486,020
East Coast				
Nova Scotia shelf	2,093,647		455,584	
Labrador shelf	2,471,595		247,159	
Grand Banks	1,463,756		537,772	
Gulf of St. Lawrence	1,144,147	7,173,145	286,038	1,526,553
Total Canada		21,005,593		9,453,985
FOREIGN				
Producing leases:				
United Kingdom		180,927		6,030
U.S.A.		20,760		1,138
Exploratory acreage:				
Australia		30,341,010		3,356,969
Indonesia - Arafura Sea		39,896,862		1,994,843
Kenya		6,669,000		1,667,250
Tunisia		2,837,430		425,575
Italy		250,550		101,089
Malta		426,218		90,571
Abu Dhabi		583,786		58,379
United Kingdom		488,502		30,472
Sicily		78,279		19,570
Netherlands		305,341		10,177
U.S.A.		97,760		3,611
Total Foreign		82,176,425		7,765,674
TOTAL ACREAGE		103,182,018		17,219,659

1973 Sales by Major Fields and Areas

	Oil (Bbls.)	Condensate (Bbls.)	L.P.G. (Bbls.)	Gas (Mcf)	Sulphur (L. Tons)	Gross Operating Revenue
Alberta						
Harmattan	2,209,909	1,160,616	485,564	16,627,143	47,103	$17,827,909
Crossfield-Carstairs	35,560	306,653	268,035	19,464,953	124,047	6,156,797
Ferrier	423,451	255,844	442,202	9,361,527	—	4,979,244
Innisfail	1,117,547	47,290	—	1,004,620	6,520	4,422,834
Pembina	953,338	2,349	—	652,741	—	3,451,528
Kaybob	—	430,393	163,426	1,612,054	32,089	2,443,327
Clive	370,172	—	—	361,251	—	1,356,136
Lone Pine Creek	—	104,795	—	4,220,037	—	1,193,284
Swan Hills	275,296	—	—	—	—	993,578
Olds	198,589	22,583	31,174	794,743	—	930,515
Cherhill	291,452	—	—	—	—	877,921
Garrington	39,838	45,437	31,649	1,370,479	—	601,246
Minnehik Buck Lake	—	25,039	—	1,819,592	—	524,010
Meekwap	144,580	—	—	—	—	502,321
Joffre	127,615	1,229	1,790	55,933	194	489,354
New Norway	133,891	—	—	—	—	484,412
Zama North	159,153	—	—	—	—	440,297
Gilby	21,497	17,715	20,424	1,305,506	—	433,141
Nevis	35,168	17,426	7,622	1,124,228	5,668	426,619
Lookout Butte	—	46,805	20,657	647,330	656	323,508
Other	540,323	53,307	32,502	5,333,103	346	2,913,542
	7,077,379	2,537,481	1,505,045	65,755,240	216,623	51,771,523
Saskatchewan						
Steelman	422,497	—	—	195,285	—	1,508,023
Weyburn	426,365	—	—	—	—	1,350,256
Midale	301,266	—	—	—	—	955,794
Other	168,935	—	—	289,771	—	617,193
	1,319,063	—	—	485,056	—	4,431,266
British Columbia						
Inga	399,097	—	—	906,547	—	1,438,791
Other	44,814	—	—	1,932,371	—	376,876
	443,911	—	—	2,838,918	—	1,815,667
Manitoba	124,749	—	—	—	—	419,338
CANADA	8,965,102	2,537,481	1,505,045	69,079,214	216,623	58,437,794
Foreign						
United Kingdom	—	10,073	—	2,906,702	—	916,784
United States	—	36,157	2,107	2,468,639	—	849,468
TOTAL	8,965,102	2,583,711	1,507,152	74,454,555	216,623	$60,204,046

Financial

Gross operating income from the sale of petroleum products amounted to $60.2 million, an increase of $15.6 million, or 35%, over the previous year. Non-operating income, including interest and dividends, increased by 53% to $2.8 million to bring the total revenue from all sources to a record high of $63 million. Cash flow before drilling and exploration expenditures amounted to $36.4 million, or $4.27 per share, compared with $3.17 per share in the prior year. Net income of $12.3 million, equivalent to $1.45 per share, provided a rate of return on invested capital of 9.5%. This compares with $6.6 million, or $.78 per share in 1972, representing a rate of return of 5.3%.

Revenue from foreign operations became more significant during 1973 with production commencing on our interests Offshore Louisiana and Texas in the Gulf of Mexico. Combined gross operating income from the United States and the United Kingdom sector of the North Sea amounted to $1.8 million.

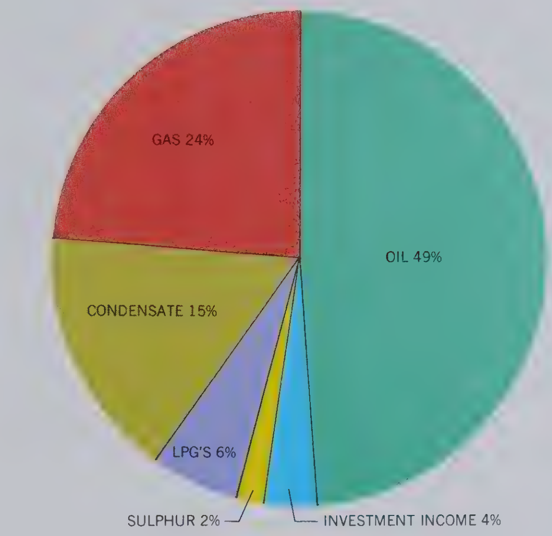
Operating, administrative and general expenses increased 23% during 1973. A significant factor in this increase was the Alberta Oil Reserves Tax imposed during 1973 which amounted to $937,000 and was charged to operating expense. This tax applied to freehold and certain Crown leases where the company elected to pay the tax rather than increased royalty. This tax, as it applies to Crown production, will be discontinued in 1974 and will be replaced by anticipated higher royalties which have not yet been announced.

Expenditures for acquisitions of properties, plant and equipment, drilling and exploration amounted to $27.1 million during the year; a decrease of $3.5 million from 1972. There was $5.2 million less spent on plant and equipment during 1973 than in 1972. Major gas plant construction in Canada has peaked out and there will be a decline in capital expenditures for plants in future years unless and until new gas discoveries are made. Expenditures on drilling and exploration remained at a high level during 1973, increasing slightly over 1972.

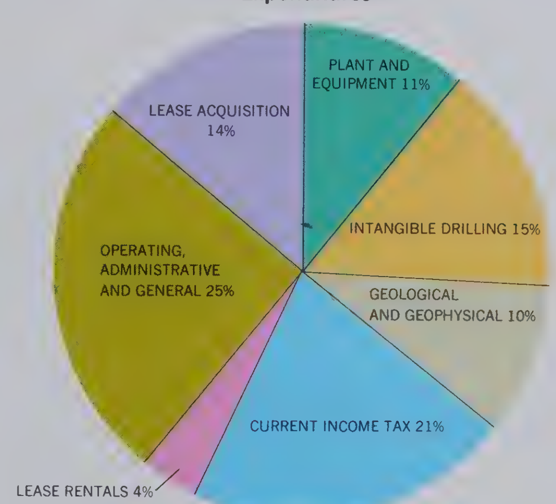
As a result of negotiations on gas price redeterminations with a gas purchaser during the year, the company repaid approximately $10 million, representing the outstanding portion of the Harmattan Area prepayments received in 1970. In spite of this large payment, the company's financial position remained strong and debt-free with working capital increasing $1.7 million to $18,636,258 at the year end.

The current portion of income taxes paid to federal and provincial governments increased from $6,315,174 to $11,060,062 in 1973. This increase of 75% is mainly a reflection of higher revenues but the relationship of

Revenues



Expenditures



taxes payable to consolidated income as reported for accounting purposes may vary from year to year. One important difference between the financial and income tax accounting relates to foreign expenditures, which, except to a limited extent, are not deductible from taxable Canadian income. During 1973 some $12.4 million was spent on lease acquisitions, exploration and development of petroleum and minerals outside of Canada, the major portion of which would have been immediately deductible for tax purposes if incurred in Canada. Another major difference relates to the costs of leases, reservations and permits acquired in Canada which can be deducted from taxable income in the year of acquisition but which are not written-off for accounting purposes until they are abandoned.

In accordance with the general practice in the Canadian oil and gas industry, the company follows the tax allocation basis to the extent of providing for deferred income tax as a result of claiming capital cost allowance for income tax purposes in excess of depreciation recorded in the accounts. Management does not consider it appropriate to provide for income tax timing differences that relate to drilling, exploration and lease acquisition costs.

During the fourth quarter of 1973, gross revenues amounted to $20.2 million, up 59% over the same period of 1972. Cash flow increased 47% to $11.6 million. Net income amounted to $5.1 million as compared with $1.7 million during the fourth quarter of 1972.

Discussions contained elsewhere in this report on exploration and development deal with the specific programs related to the company's international operations. The following table sets out the expenditures incurred in the various countries outside of Canada:

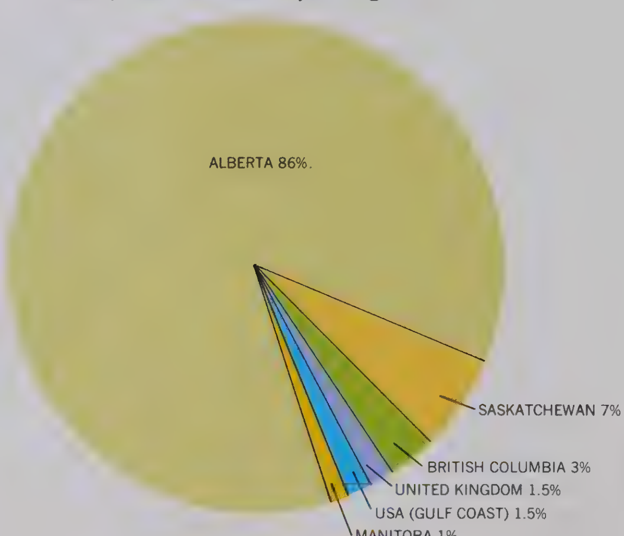
Expenditures Incurred Outside of Canada For Lease Acquisition, Exploration, Drilling and Capital Equipment

(Thousands of Dollars)

	1973	1972	1971
PETROLEUM			
United States	$ 7,845*	$ 7,854*	$ 440
Abu Dhabi	1,431	—	—
United Kingdom	698	468	69
Philippines	628	103	—
Tunisia	388	4	243
Australia	314	516	74
Peru	168	1	—
Indonesia	148	452	398
Italy	103	13	19
Turkey	89	66	11
Norway	85	127	—
Kenya	59	4	—
Trinidad	16	—	—
Malta	—	846	388
Other	61	235	56
	12,033	10,689	1,698
MINERALS			
Australia	156	180	246
United States	132	166	106
Ireland	27	—	—
Other	4	10	1
	319	356	353
	$12,352	$11,045	$ 2,051

** Includes lease acquisition costs of $5.4 million in 1973 and $6.0 million in 1972.*

Geographical Source of Operating Revenue



1973
Financial
Statements

Consolidated Statement of Income and Retained Earnings

For the Years Ended December 31, 1973 and 1972

	1973	1972
Income		
Gross operating income	$60,204,046	$44,563,118
Interest, dividends and other income	2,803,112	1,833,942
	63,007,158	46,397,060
Expenses		
Operating, administrative and general expenses	13,343,050	10,862,410
Rents of undeveloped properties	2,204,823	2,224,570
Exploration — geological and geophysical	5,405,769	4,430,172
Intangible drilling expenditures	8,282,009	7,677,867
Depreciation	5,979,364	5,825,443
Depletion	750,584	571,947
Leases abandoned	2,697,484	1,092,874
	38,663,083	32,685,283
Income Before Income Taxes	24,344,075	13,711,777
Provision for income taxes (Note 2)		
Current	11,060,062	6,315,174
Deferred	946,000	778,000
	12,006,062	7,093,174
Net Income	12,338,013	6,618,603
Retained Earnings at Beginning of Year	72,243,803	65,625,200
Retained Earnings at End of Year	$84,581,816	$72,243,803
Average Shares Outstanding	8,533,331	8,507,302
Net Income Per Share based on average number of shares outstanding	$1.45	$ .78

Canadian Superior Oil Ltd.

Consolidated Statement of Changes in Financial Position

For the Years Ended December 31, 1973 and 1972

	1973	1972
Source of Working Capital		
Net income	**$12,338,013**	$ 6,618,603
Add charges to income not requiring the use of working capital including depreciation, depletion, amortization, leases abandoned and deferred income taxes	**10,373,432**	8,268,264
	22,711,445	14,886,867
Add drilling and exploration expenditures	**13,687,778**	12,108,039
Working capital provided from operations before drilling and exploration expenditures	**36,399,223**	26,994,906
Decrease in deferred receivable	—	8,000,000
Capital stock issued for cash (Note 4)	**990,964**	335,790
Prepaid gas revenue	**1,526,090**	—
Miscellaneous	**282,892**	107,771
	39,199,169	35,438,467
Use of Working Capital		
Capital expenditures		
Lease acquisition	**7,579,429**	7,444,853
Plant and equipment	**5,839,338**	11,074,081
Exploration — geological and geophysical	**5,405,769**	4,430,172
Intangible drilling costs	**8,282,009**	7,677,867
Total capital, drilling and exploration expenditures	**27,106,545**	30,626,973
Investment in other companies	**373,993**	1,753,858
Decrease in prepaid gas revenue	**10,030,022**	1,725,741
Miscellaneous	**26,753**	118,986
	37,537,313	34,225,558
Increase in Working Capital	**1,661,856**	1,212,909
Working Capital at Beginning of Year	**16,974,402**	15,761,493
Working Capital at End of Year	**$18,636,258**	$16,974,402
Changes in Components of Working Capital		
Increase (decrease) in current assets		
Cash	**$ 872,377**	$ 87,199
Short term investments	**(3,328,052)**	14,410,802
Accounts receivable	**2,317,482**	(3,231,210)
Inventories	**305,306**	(408,379)
Current portion of deferred receivable	**(6,593,983)**	3,091,265
Net increase (decrease) in current assets	**(6,426,870)**	13,949,677
Increase (decrease) in current liabilities		
Accounts payable	**(5,716,004)**	5,107,761
Income taxes payable	**(1,071,425)**	6,079,570
Current portion of prepaid gas revenue	**(1,301,297)**	1,549,437
Net increase (decrease) in current liabilities	**(8,088,726)**	12,736,768
Increase in Working Capital	**$ 1,661,856**	$ 1,212,909

Canadian Superior Oil Ltd.

Consolidated Balance Sheet at December 31, 1973 and 1972

Assets

	1973	1972
Current Assets		
Cash	$ 1,732,797	$ 860,420
Short term investments, at cost	13,171,948	16,500,000
Accounts receivable	12,287,586	9,970,104
Inventories, at lower of cost or net realizable value		
Sulphur and liquid products	1,718,325	1,681,645
Materials and supplies	746,526	477,900
Current portion of deferred receivable	497,282	7,091,265
	30,154,464	36,581,334
Investments, at cost		
McIntyre Porcupine Mines Limited (quoted market value 1973 $4,478,531; 1972 $3,966,000)	9,005,499	9,005,499
Falconbridge Nickel Mines Limited (quoted market value 1973 $1,213,875; 1972 $1,272,500)	1,729,290	1,729,290
Other investments	3,881,788	3,507,795
	14,616,577	14,242,584
Properties, Plant and Equipment, at cost (Note 1)		
Undeveloped properties	38,378,754	36,559,260
Producing properties	22,796,744	19,734,295
Production equipment	35,906,197	35,250,559
Gas plants and related facilities	56,358,827	51,703,267
Other property and equipment	2,335,632	2,274,765
	155,776,154	145,522,146
Less: Accumulated depreciation and depletion	57,530,631	51,049,260
	98,245,523	94,472,886
Deferred Charges		
Prepaid lease rentals	987,550	1,000,496
Other	575,062	599,557
	1,562,612	1,600,053
	$144,579,176	$146,896,857

Liabilities

	1973	1972
Current Liabilities		
Accounts payable	$ 6,261,921	$ 11,977,925
Income taxes payable	5,008,145	6,079,570
Current portion of prepaid gas revenue	248,140	1,549,437
	11,518,206	19,606,932
Prepaid Gas Revenue, less current portion	2,672,339	11,176,271
Deferred Income Taxes (Note 2)	6,252,000	5,306,000
Shareholders' Equity		
Capital stock of $1 par value (Note 4)		
Authorized — 10,000,000 shares		
Issued and outstanding — 8,548,286 shares (1972 — 8,515,546)	8,548,286	8,515,546
Capital in excess of par value	31,006,529	30,048,305
Retained earnings, per accompanying statement	84,581,816	72,243,803
	124,136,631	110,807,654
Contingent Liabilities (Note 3)		
	$144,579,176	$146,896,857

Approved on behalf of the Board

A. E. Feldmeyer Director

J. W. Pyle Director

Notes to Consolidated Financial Statements

1. Accounting Policies

The consolidated financial statements include the accounts of Canadian Superior Oil Ltd. and its subsidiaries, all of which are wholly owned.

The cost of petroleum and natural gas interests are initially capitalized. Property costs are transferred from undeveloped to producing properties when production commences; costs of properties abandoned are charged against income when the properties are surrendered. Depletion of producing properties is provided by the unit of production method based on estimated recoverable reserves of oil and gas. Accumulated depletion as at December 31, 1973 amounted to $4,769,731 (1972 — $4,019,147).

Exploration expenditures and intangible drilling expenditures applicable to both producing wells and dry holes are charged to income as incurred.

Depreciation is provided by the diminishing balance method at the following rates:

Production equipment (including casing)	30%
Gas plants and related facilities	10%

Foreign currency balances included in the consolidated financial statements have been expressed in Canadian dollars on the following basis:

Current assets and liabilities - at the rate of exchange at the year end

Other assets and liabilities - at historical rates of exchange

Income and expenses - at monthly rates of exchange except provisions for depreciation and amortization which are translated on the same basis as the related assets.

2. Income Tax

The company follows the tax allocation basis of accounting for income taxes except for those timing differences that relate to drilling, exploration and lease acquisition costs. This conforms with general practice in the Canadian oil and gas industry. If the tax allocation basis had been followed for timing differences involving such costs, the deferred tax provision would have been decreased by $3,800,000 for 1973 (decreased by $1,800,000 for 1972) and increased $12,500,000 on a cumulative basis to December 31, 1973.

At the request of the Canadian provincial securities commissions, representatives of the oil and gas industry in Canada have undertaken a study to consider whether or not income tax allocation accounting as recommended by the Canadian Institute of Chartered Accountants is appropriate to the industry and to determine if an alternative method would be acceptable in certain circumstances. The commissions have indicated that unless the industry can establish an acceptable alternative, companies should be prepared to adopt tax allocation accounting with respect to drilling, exploration and lease acquisition costs effective in 1974.

3. Commitments and Contingent Liabilities

The company has a lease on office premises which expires in 1990 (with an option to renew). Under the terms of the lease the company is required to pay an annual net rental of $577,000.

The company might be required under certain conditions to make payments under guarantee and other contractual arrangements principally in connection with:

(a) pipe line transportation, and

(b) the issuing to and depositing with the federal and provincial governments of non-interest bearing demand promissory notes to be held as work performance deposits in respect of exploratory rights.

The contingent liability under such arrangements does not exceed $5,000,000 (1972 — $6,000,000).

4. Stock Options

Under the company's stock option plan, options have been granted to certain officers and key employees of the company and its subsidiaries at prices of $31.20 and $28.60 which prices were not lower than 90% of the market value on date of grant. The options are exercisable from time to time on a cumulative basis and expire in 1979.

During 1973 options on 32,740 common shares were exercised for a cash consideration of $990,964. The excess of the issue price over the par value of shares issued has been credited to capital in excess of par value. As at December 31, 1973 options for 34,330 shares (of which 27,800 were granted to directors and officers) were outstanding and 68,900 shares were available for future grants.

5. Statutory Information

During 1973 there were thirteen directors (including three past directors) and eleven officers (including two past officers) of whom seven were also directors.

Officers' remuneration and directors' fees for 1973 amounted to $485,184 and $1,000 respectively (1972 — $409,766 and $1,000), none of which were paid by subsidiary companies.

Auditors' Report

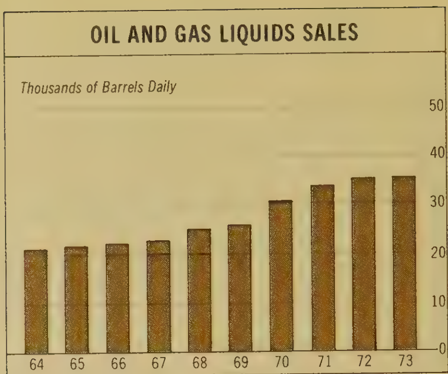
To the Shareholders of
CANADIAN SUPERIOR OIL LTD.

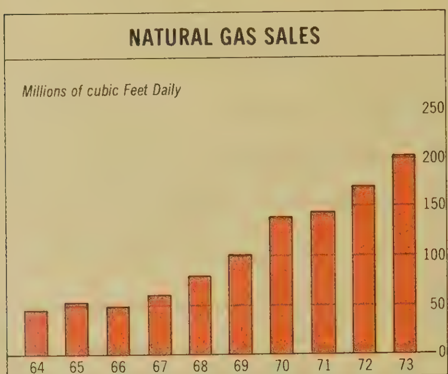
We have examined the consolidated balance sheet of Canadian Superior Oil Ltd. and its subsidiaries as at December 31, 1973 and the consolidated statements of income and retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of accounting records and such other auditing procedures as we considered necessary in the circumstances.

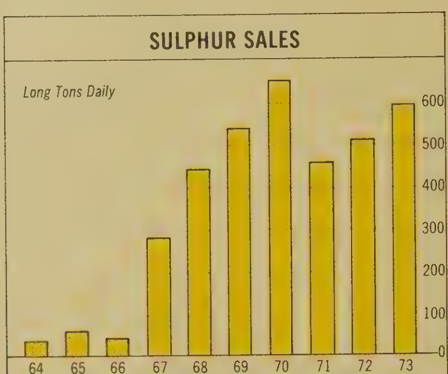
In our opinion these consolidated financial statements present fairly the financial position of the companies as at December 31, 1973 and the results of their operations and changes in their financial position for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

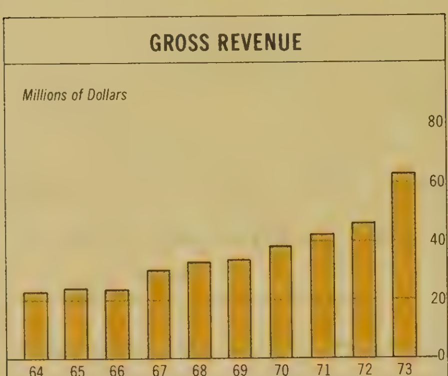
CALGARY, Alberta.
February 15, 1974

PRICE WATERHOUSE & CO.
Chartered Accountants







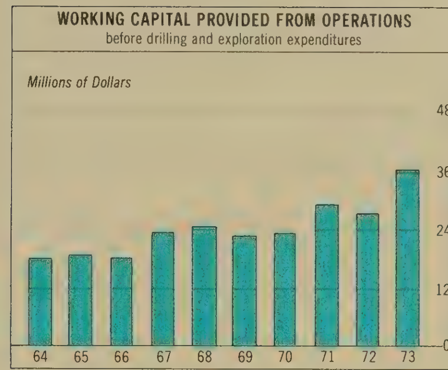


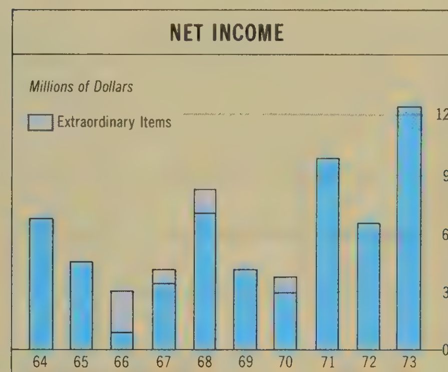
Canadian Superior Oil Ltd.

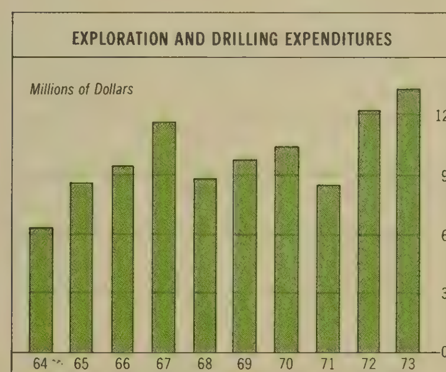
Ten Year Summary

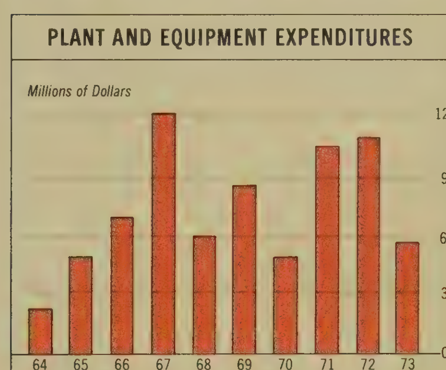
	1973	1972	1971	1970
Gross Revenue	**$63,007,158**	46,397,060	42,058,850	38,003,5
Working Capital provided from operations — *before drilling and exploration expenditures* . . .	**$36,399,223**	26,994,906	28,244,783	22,876,9
Per Share	**$4.27**	3.17	3.32	2.69
Income before extraordinary items	**$12,338,013**	6,618,603	9,783,776	2,893,6
Per Share	**$1.45**	.78	1.15	.34
Extraordinary items	—	—	—	807,4
Per Share	—	—	—	.10
Net Income	**$12,338,013**	6,618,603	9,783,776	3,701,0
Per Share	**$1.45**	.78	1.15	.44
Working Capital at Year End . . .	**$18,636,258**	16,974,402	15,761,493	17,770,0
EXPENDITURES:				
Oil and Gas Properties	**$ 7,579,429**	7,444,853	2,447,460	6,137,6
Plant and Equipment	**5,839,338**	11,074,081	10,670,311	5,012,7
Intangible Drilling	**8,282,009**	7,677,867	3,360,999	5,568,3
Exploration — Geological and Geophysical	**5,405,769**	4,430,172	5,051,583	4,829,1
	$27,106,545	30,626,973	21,530,353	21,547,8
Expenditures incurred outside of Canada included above . . .	**$12,352,468**	11,044,768	2,051,055	4,869,9
NET ACREAGE IN CANADA .	**9,453,985**	10,048,035	10,285,779	9,898,4
NET WELLS COMPLETED:				
Oil	**12.0**	5.6	4.3	12.7
Gas	**6.5**	8.1	3.5	8.7
Dry	**16.6**	29.8	17.3	19.3
	35.1	43.5	25.1	40.7
AVERAGE NET DAILY SALES:				
Crude Oil (Bbls.)	**24,562**	23,036	21,585	20,
Condensate (Bbls.)	**7,079**	7,472	6,663	6,
Propane and Butane (Bbls.) . .	**4,129**	4,609	4,220	3,
Total Oil and Gas Liquids . .	**35,770**	35,117	32,468	30,
Residue Gas (Mcf.)	**203,985**	162,632	145,097	139,
Sulphur (Long Tons)	**593**	504	449	6

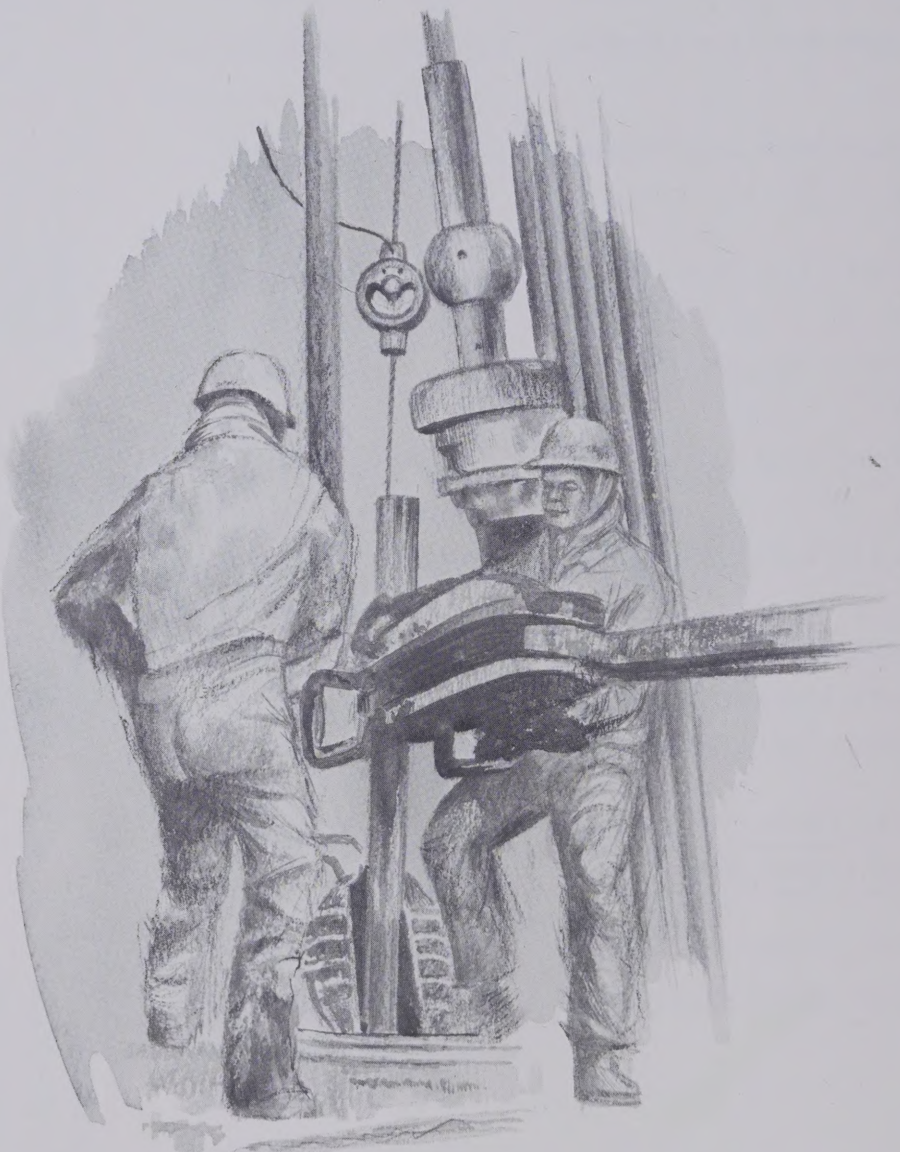
1969	1968	1967	1966	1965	1964
33,711,153	33,143,842	30,875,617	24,297,814	24,395,528	23,096,911
22,577,054	24,688,894	23,259,070	17,778,607	18,297,187	17,623,639
2.66	2.90	2.74	2.09	2.15	2.07
4,070,744	7,384,811	3,726,254	1,088,245	4,715,474	6,891,254
.48	.87	.44	.13	.55	.81
—	1,117,918	619,500	2,000,000	—	—
—	.13	.07	.23	—	—
4,070,744	8,502,729	4,345,754	3,088,245	4,715,474	6,891,254
.48	1.00	.51	.36	.55	.81
7,210,005	8,277,457	4,284,232	9,287,969	11,537,797	17,091,450
4,526,022	6,849,768	3,144,335	2,843,914	10,403,097	5,419,213
8,780,906	6,091,539	12,042,987	6,813,818	4,802,032	2,142,120
4,668,532	4,835,251	7,607,575	6,224,491	5,418,643	2,709,101
5,129,074	4,026,409	4,100,251	3,425,670	3,301,719	3,479,768
23,104,534	21,802,967	26,895,148	19,307,893	23,925,491	13,750,202
1,628,864	3,530,190	1,563,157	1,012,224	793,508	1,488,919
9,198,557	8,643,160	6,339,987	7,044,794	7,345,277	7,346,842
10.7	16.9	42.8	25.7	30.7	15.4
7.6	6.0	9.9	8.8	7.4	5.6
14.9	17.5	8.2	18.5	23.1	16.7
33.2	40.4	60.9	53.0	61.2	37.7
18,612	17,881	17,758	16,269	16,087	17,054
5,006	4,333	4,182	4,360	4,556	3,608
2,771	2,705	1,684	1,572	694	366
26,389	24,919	23,624	22,201	21,337	21,028
99,797	78,103	59,390	51,686	52,403	45,325
534	449	284	37	58	36

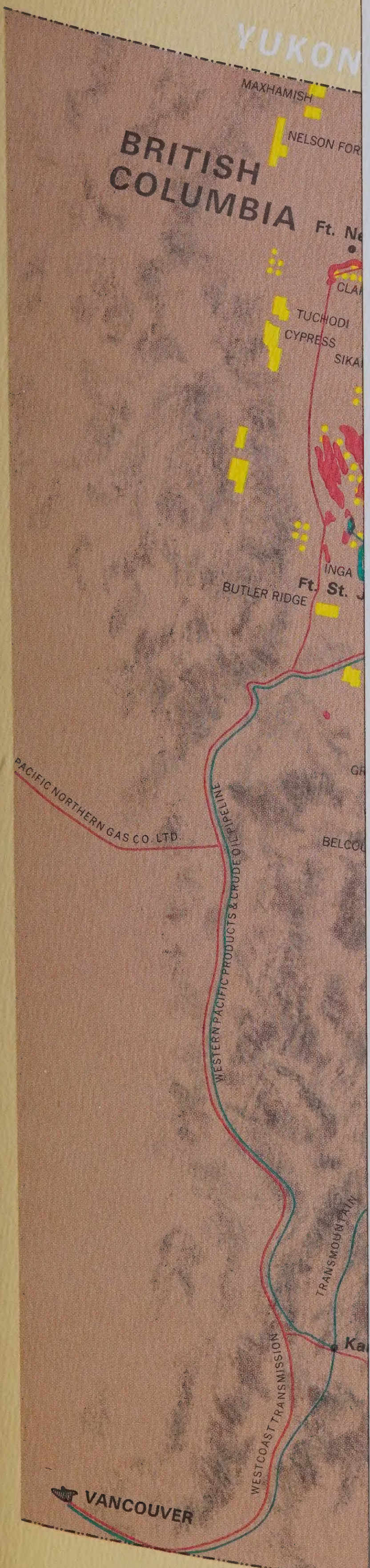












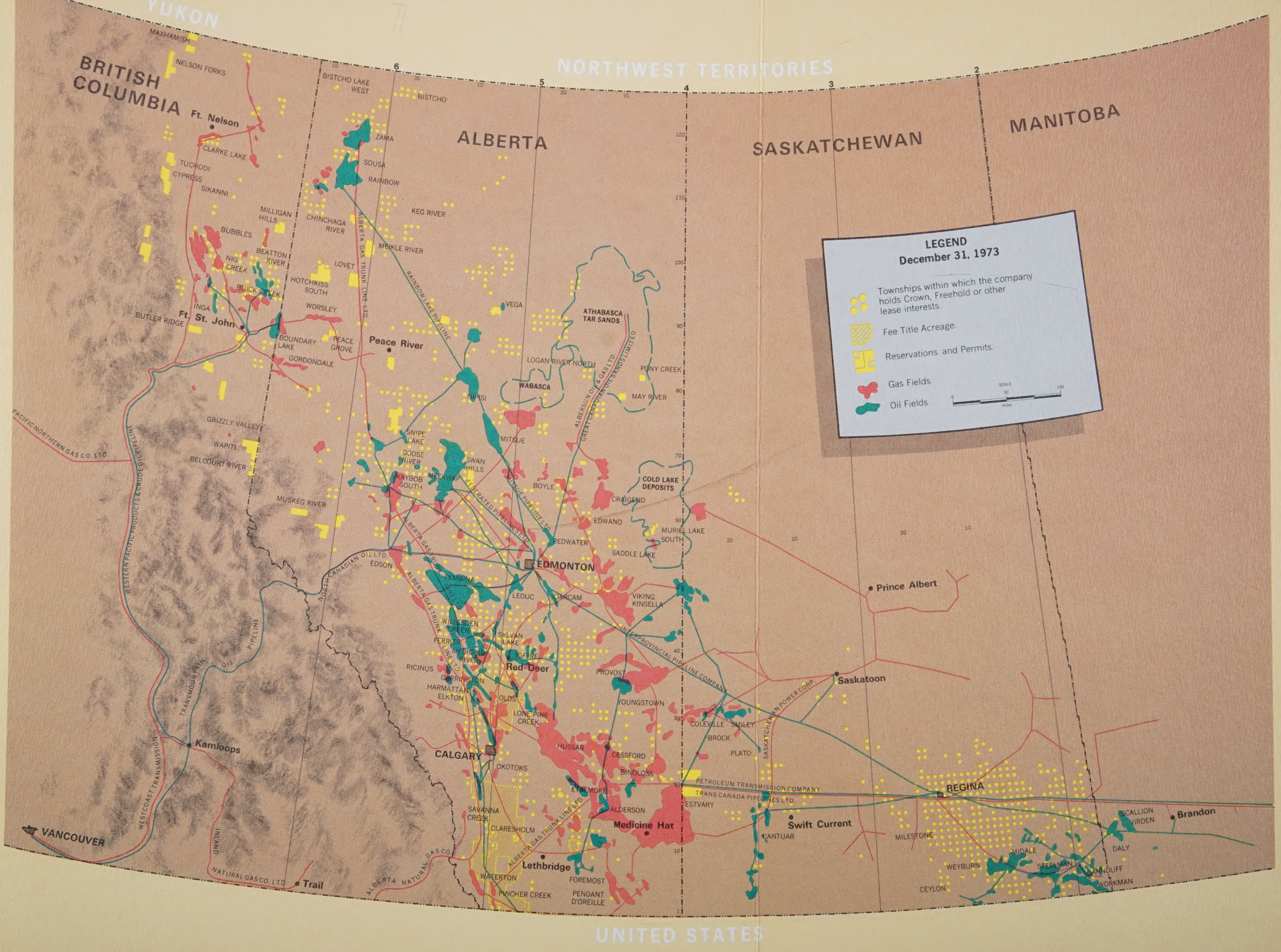
Map showing

acreage holdings

of **Canadian Superior Oil Ltd.**

1973

Canadian Superior Oil Ltd. acreage holdings in Western Provinces



SMITH GRANT MANN ALBER
Litho'd in Canada